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TAGS: [ECON](#) [EAGR](#) [CH](#)
SUBJECT: CHINA/DOMESTIC DEMAND: DON'T BET ON RURAL
CONSUMERS YET

Refs: A. Beijing 580, Beijing 589, Beijing 649

- [1](#)B. Beijing 583
- [1](#)C. Beijing 590
- [1](#)D. Beijing 614
- [1](#)E. 08 Beijing 4100
- [1](#)F. Shanghai 119

(U) This cable is Sensitive but Unclassified.
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[1](#)1. (SBU) Summary: Slumping rural income growth due to both lower agricultural prices and remittances, and a still-inadequate rural social safety net hamper Chinese Government efforts to boost rural consumption. Consumer spending coupons and rebates have had only a limited impact. Despite an emphasis on "livelihood" issues and domestic-demand-led growth at the March 5-13 National People's Congress (NPC), efforts to maintain economic growth will likely continue to rely mainly on state-led investment. End Summary.

Government Focuses on Boosting Consumption

[1](#)2. (SBU) This year's NPC focused on achieving 8 percent growth in 2009 as well as rebalancing China's economy by relying less on investment and exports and more on domestic consumption, particularly private consumption (Ref A). Reflecting long-standing concerns about China's growth model, Premier Wen Jiabao's Government Work Report stated that China "needs to vigorously expand domestic demand, particularly consumer demand." Ministry of Agriculture (MoA) public documents stated that "rural areas have the greatest potential for expanding domestic demand" and that "the focus for ensuring improved livelihoods ... is on farmers."

Government is Acting

[1](#)3. (SBU) To address the need to boost consumption in the near term, Wen's Work Report said the Government will "promptly work out and introduce policies and measures to encourage consumption and vigorously develop consumer credit" and make home appliances, agricultural machinery, and automobiles and

motorbikes affordable to rural residents. The Government has implemented "Appliances to the Countryside" programs (see Ref B) and according to Ministry of Commerce (MOFCOM) Beijing will provide 20 billion yuan (almost USD 3 billion) in subsidies in 2009 to boost appliance sales in rural areas. On March 12, an official said that MoA will expand existing subsidy programs to boost farm equipment purchases, which he argued are important not only to boosting agriculture productivity, but also because farm machinery sales and repair provide off-farm employment. Local governments are also providing consumer spending coupons to targeted rural and low-income residents (see Ref C), although it is doubtful the Central Government will make this a nationwide policy.

But Lagging Rural Incomes Pose Challenge

14. (SBU) Vice Minister of Agriculture Wei Chao'an said in a March 12 press conference on the margins of the NPC that although farmers are key to boosting domestic demand, "farmers' situation also makes this difficult." Wei admitted that it would be difficult to maintain the growth of real per capita rural incomes in 2009 at the same six to eight percent levels achieved over the previous five years. (Note: real per capita rural income growth was eight percent in 2008. End Note.) According to Wei the difficulties are the result of the global financial

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crisis, which is causing lower agricultural commodity prices, weaker agricultural exports, a tough business environment for non-farm rural enterprises, and job losses among migrant workers. (Comment: According to official data around half of rural incomes are derived from off-farm work. It is unlikely that new jobs in government-backed infrastructure projects will fully offset unemployment resulting from slowdowns in the labor-intensive exporting and property sectors. The People's Bank of China's Quarterly Monetary Policy Report stated that rural spending is more sensitive to both positive and negative changes in income. End Comment.)

And Changing Spending Behavior Takes Time

15. (SBU) Consumer retail spending numbers in China have held up relatively well; retail sales increased 15 percent in January and February over the same period last year. This increase, however, is much lower than in recent years and was pumped up by government purchases. Also, the rate of retail sales growth is slowing when viewed on a month-to-month basis. The real impact of the downturn on consumption growth could be seen most clearly in the appliance sales figures, which increased less than 3 percent despite the plethora of programs designed to spur spending in this sector. World Bank China Country Director David Dollar and other economists point out that a near term private consumption boost to the economy is unlikely. According to a March 13 blog article by Dollar, "consumption habits are not going to change overnight." (See also Ref D)

16. (SBU) Xiao Geng, a macroeconomist and Director of the Brookings-Tsinghua Center for Public Policy in Beijing, claims consumption is unlikely to account for a larger share of economic growth given current circumstances. In a February 18 meeting with Econoffs Geng noted that individuals still need to save money for healthcare and their children's

education, and individuals earn little from their financial assets because of the still undeveloped financial system, which both leads to high precautionary savings as households are forced to self-insure and contributes to a growth of household income which has lagged behind broader economic growth. Xiao said the financial system as well as the pension, education, and healthcare systems will only improve gradually. Land experts such as Li Ping from the Rural Development Institute also point out that slow progress toward privatizing rural land also hampers rural consumption (Ref E). The PBOC noted in its Quarterly Monetary Policy Report that, because of the weak social safety net and other factors, since 2002 consumption spending of both urban and rural households has become less responsive to changes in income. (See also Ref F)

17. (SBU) Xiao also commented that consumer spending coupons and rebates may not work well because consumers will offset spending using coupons or other incentive programs with other spending, thus maintaining the same overall level of spending and savings. Other contacts point out that many consumers will find ways to turn consumer spending coupons into cash through black market schemes and then save the cash.

Comment: Rural Consumption Won't Save China

18. (SBU) Beijing is clearly committed to increasing rural incomes and consumption, but this is a long-term project that will take years to bear fruit. With their high sensitivity to income effects, rural residents are likely to reduce spending during an economic downturn, especially one likely to impact

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migrant labor employment prospects. China's efforts to boost rural consumption through ad hoc subsidies and incentives may have some impact on the margins, but cannot overcome the larger effect of rising uncertainty and declining incomes. Over the next few years, China will have to look elsewhere for economic engines to pull domestic growth.

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